Statement

By

The Alliance of American Insurers

Submitted for the Hearing Record

Before

The Senate Commerce, Science and Transportation Committee

April 13, 2000

Hearing on

S 1361

The Natural Disaster Protection and Insurance Act

The Alliance of American Insurers is a national property and casualty insurance trade association representing more than 300 companies. Alliance membership is diverse, representing large multi-line insurers doing business in all states as well as small regional and single state insurance companies. We offer the following comments on S.1361, a bill to amend the Earthquake Hazards Reduction Act of 1977.

For more than two decades the Alliance has participated in discussions regarding a federal response to property losses from natural catastrophes. While we have supported congressional action for flood insurance and commend Senator Stevens for his effort in developing this legislation, we do not believe S.1361 is either appropriate or necessary.

We believe the current capacity of the reinsurance industry, both domestic and offshore, is sufficient to meet the needs of our domestic property and casualty industry. Access to the capital markets via "securitization", as well as the development and use of other sophisticated risk transfer mechanisms, is functioning well to supplement traditional reinsurance. The successful placement of catastrophe bonds has expanded the industry's capacity to provide coverage. The legislation's encouragement of state programs and the creation of a federal reinsurance program strikes at the core of our belief that the private insurance market offers better, and more creative, responses to questions about the industry's ability to respond to natural disasters.

Creation of a Natural Disaster Insurance Corporation, as required by this act, would establish a private reinsurer that would have the ability to raise funds through the auspices of the Department of the Treasury. While the stated purpose in S.1361 is not to compete or supplant private markets, this is exactly what the bill would do.

The bill allows state funds to collect reinsurance funds for loss occurrences not less that the greater of $2 billion or the "claims-paying capacity of the eligible State program." The Alliance believes S.1361 would thereby encourage the creation of more state catastrophe programs in order to take advantage of federal reinsurance.

While S.1361 does contain extensive provisions for mitigation, the Alliance is concerned that they do not adequately address the issue of overbuilding in catastrophe-prone regions of the country. The bill calls for a study of this issue by states, but does not require any action to limit the concentration of risk. Land use and zoning controls are needed, not increased exposures.

For example, modest coastal cottages along the eastern seaboard are being replaced with luxury homes and high rise condominiums. Following the construction of these properties, the owners of these properties expect the same continued access to inexpensive insurance coverage as though they were located in a far less hazardous area.

S.1361 does nothing to address this continued expectation that people can build what and where they want with no consequences for this action. The bill does provide for the establishment of building code requirements and enforcement of those standards by states. However, we think that the funding incentive for these programs, 10% of investment income from the Corporation funds, is inadequate.

The Alliance believes that the creation of a federal reinsurance program and the likely growth of state pools will place a continued burden on the U.S. taxpayer and private insurance policyholder to subsidize property insurance rates for people who choose to locate in catastrophe-prone areas.

Under the Stafford Act, we continue to pay federal disaster relief to public entities that do not undertake mitigation activities to improve the survivability of their properties and often do not purchase insurance or set aside funds in a self-insurance program. This continued federal largesse acts as an incentive not to mitigate and not to insure. S.1361 does contain provisions for a study of retrofitting of these properties. However, the level of mitigation funding makes it unlikely that improvement will occur.

The Alliance opposes S.1361 because it would continue to perpetuate the cycle of insurance rate subsidization of residents in hazard-prone areas and the continued overbuilding in these same areas of the country. While we can support pursuing a national mitigation policy, in our opinion, the imposition of a federal reinsurance program would not be an equitable trade-off.

The market place has responded to the perceived insurance capacity problems as they relate to natural disasters. Market solutions are almost always preferable when responding to a perceived problem. We believe this is clearly the case in this instance.